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No. 76-58

In the Supreme Court of the United States

OCTOBER TERM, 1976

SAMUEL H. SLOAN, SAMUEL H. SLOAN & Co.,
PETITIONERS

v.

SECURITIES AND EXCHANGE COMMISSION, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

**BRIEF FOR THE
SECURITIES AND EXCHANGE COMMISSION
IN OPPOSITION**

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OPINIONS BELOW

The opinion of the court of appeals, as amended (Pet. App. 1a-5a, 6a-7a), is reported at 535 F. 2d 676. The district court filed no written opinion; its oral statement is set forth at Pet. App. 9a-19a.

JURISDICTION

The judgment of the court of appeals was entered on March 4, 1976 (Pet. App. 1a) and amended on April 16, 1976, when a timely petition for rehearing was denied (Pet. App. 6a-7a). The petition for a writ of certiorari was filed on July 15, 1976. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTIONS PRESENTED

1. Whether the district court properly dismissed petitioners' challenge to the constitutionality of the Securities Exchange Act of 1934 and certain regulations thereunder.

2. Whether the constitutional claims stated in the complaint required the convening of a three-judge court.

STATUTES AND RULES INVOLVED

Petitioners have purported to challenge the constitutionality of the Securities Exchange Act of 1934 in its entirety, and all of the rules promulgated thereunder, in addition to asserting constitutional and other claims with respect to various statutory provisions and rules enumerated in their petition (Pet. 6-7). Certain of these provisions and rules are set forth in the appendix hereto.

STATEMENT

Petitioners seek review of a judgment of the Court of Appeals for the Second Circuit affirming the dis-

missal of petitioners' complaint against the Securities and Exchange Commission and other defendants. Petitioners' complaint, which sought to have the Securities Exchange Act and all rules promulgated thereunder declared unconstitutional and other relief, was filed on June 27, 1974. At that time petitioners were the subject of an administrative proceeding before the Securities and Exchange Commission, initiated pursuant to Sections 15(b)(5) and (7) of the Securities Exchange Act of 1934, 48 Stat. 881, 895, as amended, (15 U.S.C. 78o(b)(5) and (7)), to determine whether the broker-dealer registration of Sloan & Co. should be revoked and Mr. Sloan barred from association with securities brokers and dealers.¹ Petitioners also had been permanently enjoined, after a trial, from violating the recordkeeping and net capital requirements of Sections 17(a) and 15(c)(3) of the Securities Exchange Act, 15 U.S.C. 78q(a) and 78o(c)(3), and certain rules promulgated thereunder.²

¹ On April 28, 1975, the Commission issued an order, after a hearing, which revoked the firm's broker-dealer registration and barred Mr. Sloan from association with any broker or dealer. Securities Exchange Act Release No. 11376. That order is presently before the court of appeals on petition for review. *Samuel H. Sloan d/b/a Samuel H. Sloan & Co. v. Securities and Exchange Commission* (C.A. 2, No. 75-4087).

² The permanent injunction was entered on January 7, 1974. *Securities and Exchange Commission v. Samuel H. Sloan and Samuel H. Sloan & Co.*, 369 F. Supp. 996 (S.D. N.Y.). Petitioners' appeal from the permanent injunction was dismissed by the court of appeals on January 7, 1976 (C.A. 2, No. 74-1436). Mr. Justice Marshall subsequently

Petitioners' amended complaint was filed on October 22, 1974, following a determination by the district court that the original complaint was "too vague and lacking in specifics" (C.A. App. 16).³ The amended complaint may be summarized as follows:

Count I

Count I (C.A. App. A58-A59) seeks declaratory relief based on petitioners' broad assertions that the Securities Exchange Act and all of the rules and

granted petitioners an extension of time until September 10, 1976, to file a petition for a writ of certiorari.

On January 17, 1975, in another action brought by the Commission, petitioners were preliminarily enjoined from violating Section 15(c)(2) of the Securities Exchange Act, 15 U.S.C. 78o(c)(2), and Rule 15c2-11 promulgated thereunder, 17 C.F.R. 240.15c2-11 (antimanipulative rule respecting publication of quotations). Petitioners also were ordered to permit the Commission immediately to examine their books and records, as required by Section 17(a) of the Securities Exchange Act, 15 U.S.C. 78q(a), and Rule 17a-4, promulgated thereunder, 17 C.F.R. 240.17a-4. *Securities and Exchange Commission v. Samuel H. Sloan, individually and d/b/a Samuel H. Sloan & Co.* (S.D.N.Y., No. 74 Civ. 5729 (RJW)). Petitioners' appeal from this preliminary injunction was dismissed by the court of appeals on January 7, 1976 (C.A. 2, No. 75-7056), and Mr. Justice Marshall granted petitioners an extension of time until September 10, 1976, to file a petition for a writ of certiorari in that case.

Mr. Sloan, on September 3, 1975, was adjudged in civil contempt of the January 17, 1975, preliminary injunction. On May 10, 1976, the court of appeals dismissed in part an appeal from that order and affirmed the rulings of the district court in all other respects (535 F.2d 679 (C.A. 2)).

On August 18, 1976, the district court dismissed the underlying injunctive action as moot.

³ "C.A. App." refers to the appendix in the court of appeals, a copy of which is being lodged in this Court.

regulations promulgated thereunder are unconstitutional. Count I alleges that the Commission's rule-making authority under the Securities Exchange Act represents an unconstitutional delegation of authority by Congress and the President prohibited by Article I, Section 1 of the Constitution. The first count also asserts, in conclusory terms, that the Act as a whole, and the entire body of rules promulgated under the Act, are unconstitutionally vague and uncertain; violate provisions of the Bill of Rights and the Fourteenth Amendment; violate the right of contract and other unspecified Constitutional rights; and exceed the boundaries of the commerce clause.

The first count specifically attacks Section 27 of the Securities Exchange Act, 15 U.S.C. 78aa, as unconstitutional because, by reposing exclusive jurisdiction in the federal courts of all actions brought under that Act and the rules thereunder, it allegedly interferes with the jurisdiction of state courts, and because it violates other unspecified rights. Constitutional challenges are also made with respect to Sections 15(c)(5) and 19(a)(4) of the Securities Exchange Act, 15 U.S.C. 78o(c)(5) and 78s(a)(4) (summary trading suspension power);⁴ Commission Rule 15c2-11, 17 C.F.R. 240.15c2-11 (antimanipula-

⁴ Review of the Commission's summary trading suspension power is currently pending in the court of appeals. *Samuel H. Sloan v. Securities and Exchange Commission* (C.A. 2, No. 76-4110). An earlier challenge was involved in *Samuel H. Sloan v. Securities and Exchange Commission*, 527 F. 2d 11 (C.A. 2), certiorari denied, No. 75-1507, June 14, 1976.

tive rule respecting publication of quotations); Commission Rule 15c3-1, 17 C.F.R. 240.15c3-1 (broker-dealer net capital rule); Commission Rule 17a-5, 17 C.F.R. 240.17a-5 (reporting requirements for broker-dealers); and Section 12(g) of the Securities Exchange Act, 15 U.S.C. 78l(g) (reporting requirements for certain issuers of securities). These challenges generally reiterate the general allegations already noted.

Count II

In Count II (C.A. App. A59-A61) petitioners seek money damages and declaratory relief with respect to certain alleged acts by the Commission and members of its staff, who were not named as defendants. Petitioners assert that these activities—including the Commission's suspension of trading in certain securities and its refusal to accept certain amendments to Sloan & Co.'s broker-dealer registration—were unconstitutional, arbitrary, capricious and abusive of delegated authority. Count II also challenges on these grounds the Commission's promulgation or interpretation of Rule 17a-5, which requires broker-dealers to submit certified financial statements on the Commission's Form X-17A-5, and Rule 15c3-1, which requires broker-dealers to adjust their net capital, *inter alia*, to reflect the fact that trading has been suspended in securities in which they hold positions.

Count III

While the introductory language of Count III (C.A. App. A61-A63) names the Securities and Exchange

Commission with the other defendants in connection with alleged violations of the Sherman and Clayton Acts, no specific conduct on the part of the Commission is alleged in Count III and no specific relief is requested against the Commission in that count.

Count IV

Count IV (C.A. App. A63-A64) is purportedly an action based upon common law fraud, as well as Section 10(b) of the Securities Exchange Act, 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5. It alleges in conclusory terms that the Commission acted fraudulently in failing to give adequate and accurate reasons for suspending trading in securities and in discouraging, in some unspecified way, broker-dealers from entering quotations in the "pink sheets" published by the National Quotation Bureau, Inc.

Count V

Count V (C.A. App. A64) asserts in conclusory terms that petitioners are entitled to damages of \$200,000 as a result of unspecified information allegedly given by an unspecified employee of the Commission to an employee of the National Association of Securities Dealers.

In their *ad damnum*, petitioners seek judgment of \$29,600,000, and a declaratory judgment that the Securities Exchange Act and all the rules promulgated thereunder are unconstitutional and that certain acts of the Commission were unconstitutional,

arbitrary, capricious, and abusive of delegated authority.

On motion of the Commission to dismiss the complaint or in the alternative for summary judgment (C.A. App. A139) and on petitioners' cross-motion to enjoin the Commission from instituting and prosecuting actions under the Securities Exchange Act and for other relief summarized at page 10 of the petition, the district court dismissed the complaint (Pet. App. 9a-19a).

The court of appeals affirmed, characterizing petitioners' arguments as frivolous (Pet. App. 1a-5a).

ARGUMENT

1. The court of appeals, in an opinion on which we rely, properly characterized as "frivolous" (Pet. App. 4a) petitioners' "blunderbuss attack" on the constitutionality of the Securities Exchange Act and various provisions and rules promulgated thereunder. The court correctly determined that the challenged provisions of the Act and the Commission's rules thereunder "are valid and reasonable exercises of congressional power under the commerce clause and the SEC's delegated regulatory power, which infringe no constitutional rights of plaintiff" (Pet. App. 4a). No further review of this issue is warranted.

2. The court of appeals was not required "to remand the action to the district court with instructions to convene a three-judge court" (Pet. 17). A three-judge court need not be convened "when the consti-

titutional attack * * * is insubstantial," *Goosby v. Osser*, 409 U.S. 512, 518. Here, the constitutional attack upon the Securities Exchange Act and other related allegations were "patently without merit," *Bell v. Hood*, 327 U.S. 678, 683, and could be dismissed by a single district judge. See also *Hagans v. Lavine*, 415 U.S. 528.⁵

3. Petitioners' antitrust attacks appear to be based, in part at least, on the cooperation of the National Quotation Bureau, Inc., in enforcing the Commission's Rule 15c2-11 (Pet. 8-9, 15, 25). This rule defines as a "fraudulent, manipulative and deceptive practice" the publication by a broker-dealer of quotations for securities about which current data is not available—a rule that is within the scope of Section 15(c)(2) of the Act, authorizing the Commission to define (a) "fraudulent, deceptive or manipulative" acts and practices of securities brokers and dealers and (b) quotations that are "fictitious." Moreover, the court of appeals properly concluded that "none of the actions charged constitute antitrust violations, essentially because they were taken pursuant to the scheme of securities regulation established by the Securities Exchange Act of 1934. See generally, *United States v. National Association of Securities Dealers, Inc.*, 422 U.S. 694 (1975); *Gordon v. New*

⁵ Moreover, petitioners sought relief against the Commission *eo nomine* (as distinguished from bringing the action against individual commissioners allegedly acting in excess of their authority); the district court therefore was without jurisdiction respecting the charges against the Commission. *National Labor Relations Board v. Nash-Finch Co.*, 404 U.S. 138, 146, n. 4; *Holmes v. Eddy*, 341 F.2d 477, 480 (C.A. 4).

York Stock Exchange, 422 U.S. 659 (1975)" (Pet. App. 5a).

4. The court of appeals also correctly held that petitioners' remaining arguments were without merit (Pet. App. 5a, n. 5). None of these issues warrants consideration by this Court.

CONCLUSION

For the foregoing reasons the petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER 1976.

APPENDIX A

Prior to Securities Acts Amendments of 1975, which became effective on June 4, 1975, Section 15 (c) (2) of the Securities Exchange Act of 1934, as added, 52 Stat. 1075, 15 U.S.C. 78o(c) (2), provided as follows:

No broker or dealer shall make use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, in connection with which such broker or dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation. The Commission shall, for the purposes of this paragraph, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitious.

The amended Section 15(c) (2), Pub. L. 94-29, 89 Stat. 125, 15 U.S.C. (Supp. V) 78o(c) (2), now provides:

No broker or dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange of which it is a member, in connection with which such broker or dealer en-

gages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation, and no municipal securities dealer shall make use of the mails or any means or instrumentality of interstate commerce to effect any transaction in, or to induce or attempt to induce the purchase or sale of, any municipal security in connection with which such municipal securities dealer engages in any fraudulent, deceptive, or manipulative act or practice, or makes any fictitious quotation. The Commission shall, for the purposes of this paragraph, by rules and regulations define, and prescribe means reasonably designed to prevent, such acts and practices as are fraudulent, deceptive, or manipulative and such quotations as are fictitious.

APPENDIX B

Commission Rule 15c2-11, 17 C.F.R. 240.15c2-11, provides as follows:

§ 240.15c2-11 Initiation or resumption of quotations without specific information.

(a) It shall be a fraudulent, manipulative, and deceptive practice within the meaning of section 15(c)(2) of the Act, for a broker or dealer to publish any quotation for a security or, directly or indirectly, to submit any such quotation for publication, in any quotation medium (as defined in this section) unless:

(1) The issuer has filed a registration statement under the Securities Act of 1933 which became effective less than 90 calendar days prior to the day on which such broker or dealer publishes or submits the quotation to the quotation medium: *Provided*, That such registration statement has not thereafter been the subject of a stop order which is still in effect when the quotation is published or submitted, and such broker or dealer has in his records a copy of the prospectus specified by section 10(a) of the Securities Act of 1933: or

(2) The issuer has filed a notification under Regulation A under the Securities Act of 1933 which became effective less than 40 calendar days prior to the day on which such broker or dealer publishes or submits the quotation to the quotation medium: *Provided*, That the offering circular provided for under Regulation A has not thereafter become the subject of a suspension order which is still in effect when the quotation

is published or submitted, and such broker or dealer has in his records a copy of such offering circular; or

(3) (i) The issuer is required to file reports pursuant to section 13 or 15(d) of the Act, or is the issuer of a security covered by section 12(g) (2) (B) or (G) of the Act, and

(ii) The broker or dealer has a reasonable basis for believing that the issuer is current in filing the reports required to be filed at regular intervals pursuant to section 13 or 15(d) of the Act, or, in the case of insurance companies exempted from section 12(g) of the Act by section 12(g) (2) (G) thereof, the annual statement referred to in section 12(g) (2) (G) (i) of the Act; and

(iii) The broker or dealer has in his records the issuer's most recent annual report filed pursuant to section 13 or 15(d) of the Act, or the annual statement in the case of an insurance company not subject to section 12(g) of the Act, together with any other reports required to be filed at regular intervals under such provisions of the Act which have been filed by the issuer after such annual report or annual statement; or

(4) Such broker or dealer has in his records, and shall make reasonably available upon request to any person expressing an interest in a proposed transaction in the security with such broker or dealer, the following information (which shall be reasonably current in relation to the day the quotation is submitted), which he has no reasonable basis for believing is not true and correct or reasonably current, and which was obtained by him from sources which he has a

reasonable basis for believing are reliable: (i) The exact name of the issuer and its predecessor (if any); (ii) the address of its principal executive offices; (iii) the state of incorporation, if it is a corporation; (iv) the exact title and class of the security; (v) the par or stated value of the security; (vi) the number of shares or total amount of the securities outstanding as of the end of the issuer's most recent fiscal year; (vii) the name and address of the transfer agent; (viii) the nature of the issuer's business; (ix) the nature of products or services offered; (x) the nature and extent of the issuer's facilities; (xi) the name of the chief executive officer and members of the board of directors; (xii) the issuer's most recent balance sheet and profit and loss and retained earnings statements; (xiii) similar financial information for such part of the 2 preceding fiscal years as the issuer or its predecessor has been in existence; (xiv) whether the broker or dealer or any associated person is affiliated, directly or indirectly with the issuer; (xv) whether the quotation is being published or submitted on behalf of any other broker or dealer, and, if so, the name of such broker or dealer; and (xvi) whether the quotation is being submitted or published directly or indirectly on behalf of the issuer, or any director, officer or any person, directly or indirectly the beneficial owner of more than 10 percent of the outstanding units or shares of any equity security of the issuer, and, if so, the name of such person, and the basis for any exemption under the federal securities laws for any sales of such securities on behalf of such person. If such information is

made available to others upon request pursuant to this subparagraph, such delivery, unless otherwise represented, shall not constitute a representation by such broker or dealer that such information is true and correct, but shall constitute a representation by such broker or dealer that the information is reasonably current in relation to the day the quotation is submitted, that he has no reasonable basis for believing the information is not true and correct, and that the information was obtained from sources which he has a reasonable basis for believing are reliable.

(b) With respect to any security the quotation of which is within the provisions of this section, the broker or dealer submitting or publishing such quotation shall maintain in his records information regarding all circumstances involved in the submission or publication of such quotation, including the identity of the person or persons for whom the quotation is being submitted or published and any information regarding the transaction provided to the broker or dealer by such person or persons.

(c) The broker or dealer shall maintain in writing as part of his records the information described in paragraphs (a) and (b) of this section, and any other information (including adverse information) regarding the issuer which comes to his knowledge or possession before the publication of [sic] submission of the quotation, and preserve such records for the periods specified in § 240.17a-4.

(d) For any security of an issuer included in paragraph (a)(4) of this section, the broker or dealer submitting the quotation shall furnish to

the inter-dealer quotation system (as defined in paragraph (e)(1) of this section), in such form as such system shall prescribe, at least 2 days before the quotation is published or submitted, the information regarding the security and the issuer which such broker or dealer is required to maintain pursuant to said paragraph (a)(4) of this section.

(e) For purposes of this section:

(1) "Quotation medium" shall mean any "interdealer quotation system" or any publication or electronic communications network or other device which is used by brokers or dealers to make known to others their interest in transactions in any security, including offers to buy or sell at a stated price or otherwise, or invitations of offers to buy or sell.

(2) "Interdealer quotation system" shall mean any system of general circulation to brokers or dealers which regularly disseminates quotations of identified brokers or dealers.

(3) Except as otherwise specified in this section, "quotation" shall mean any bid or offer at a specified price with respect to a security.

(f) The provisions of this section shall not apply to:

(1) The publication or submission of a quotation respecting a security admitted to trading on a national securities exchange and which is traded on such an exchange on the same day as, or on the business day next preceding, the day the quotation is published or submitted.

(2) The publication or submission of a quotation for securities of foreign issuers exempt from

section 12(g) of the Act by reason of compliance with the provisions of § 240.12g3-2(b).

(3) The publication or submission of a quotation respecting a security which has been the subject of both bid and ask quotations in an inter-dealer quotation system at specified prices on each of at least 12 days within the previous 30 calendar days, with no more than 4 business days in succession without such a two-way quotation.

(g) The requirement in paragraph (a)(4) of this section that the information with respect to the issuer be "reasonably current" will be presumed to be satisfied, unless the broker or dealer has information to the contrary, if:

(1) The balance sheet is as of a date less than 16 months before the publication or submission of the quotation, the statements of profit and loss and retained earnings are for the 12 months preceding the date of such balance sheet, and if such balance sheet is not as of a date less than 6 months before the publication or submission of the quotation, it shall be accompanied by additional statements of profit and loss and retained earnings for the period from the date of such balance sheet to a date less than 6 months before the publication or submission of the quotation.

(2) Other information regarding the issuer specified in paragraph (a)(4) of this section is as of a date within 12 months prior to the publication or submission of the quotation.

(h) This section shall not prohibit any publication or submission of any quotation if the Commission, upon written request or upon its

own motion, exempts such quotation either unconditionally or on specified terms and conditions, as not constituting a fraudulent, manipulative or deceptive practice comprehended within the purpose of this section.